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Next Steps on the review of the gas interconnectors

Nathan Macwhinnie
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Why?

- Call for Evidence October 2012 because:
  - Growing importance of non-domestic gas supplies
  - EU Target Model and regulators commitment to review gas flows on their interconnectors
  - Initial analysis showed gas not always flowing to the highest priced market

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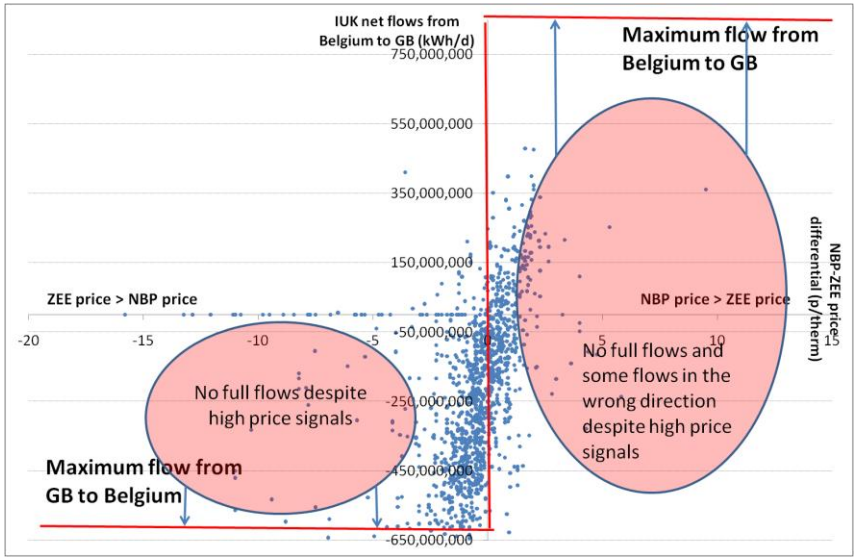
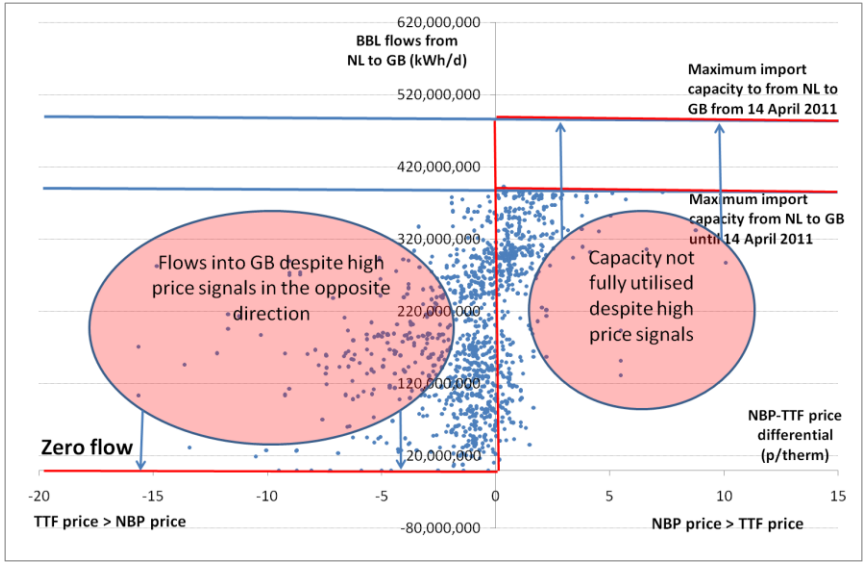
Initial findings

IUK



- On 28% of days gas flowed on IUK from the high-priced to the low-priced market, i.e. against price differentials.
- The average utilisation rate of IUK was only 38%.

BBL

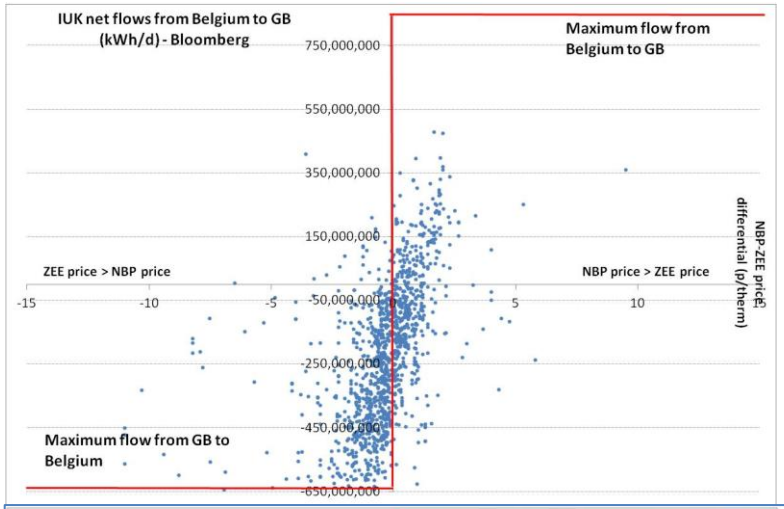


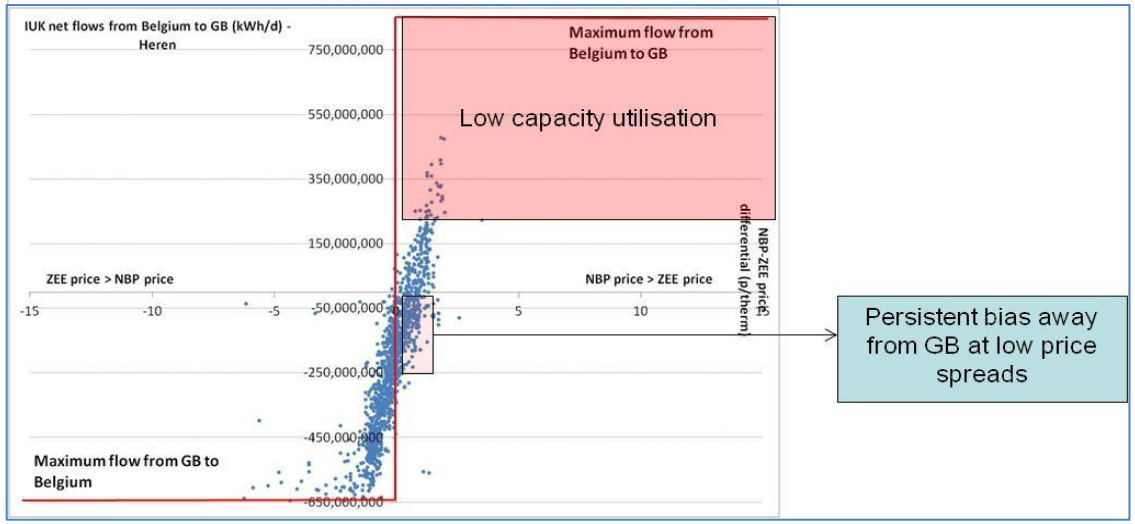
- On 65% of days, gas flowed from the Netherlands to Britain despite NBP prices being below TTF prices
- The average physical utilisation rate of BBL between 2009 and June 2012 was 47%

Stakeholder Feedback

1. Respondents do not have a concern with the price responsiveness of the interconnectors and their own work in this area. That IUK is working efficiently, supported by IUK analysis.
2. A different data source (ICIS Heren not Bloomberg) should be used
3. GB transmission charging: specifically it was argued that the commodity charge causes a bias to flows
4. The high cost of short term capacity in the Netherlands
5. Long-term contracts are mentioned by three shippers as a reason that flows may not appear to be economically logical
6. Two stakeholders note that a lack of liquidity at Zeebrugge can sometimes be an issue for traders looking to maximise cross-border trade
7. Two respondents note that the use of BBL as a Dutch balancing tool causes flow inefficiency

IUK Further Analysis (1)





Data source does have an impact.

Shows responsiveness of Shippers.

However, point still holds that, FAPD on 27% of days ...

The commodity charge effect -> gas away from the NBP

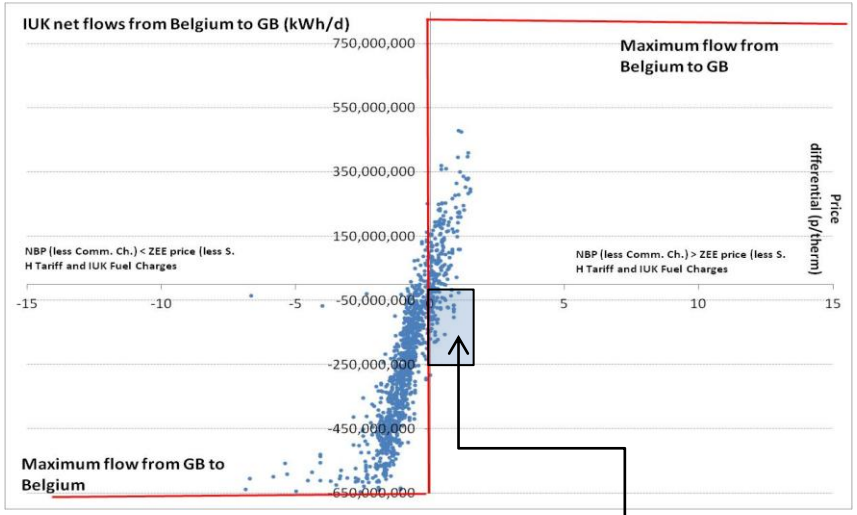
- Why?
  - Assuming a shipper has capacity (at Bacton and on IUK) a shipper can choose to pay entry commodity charges (relatively high) or the short haul tariff and IUK Fuel Charges (relatively low) and flow to ZEE ...

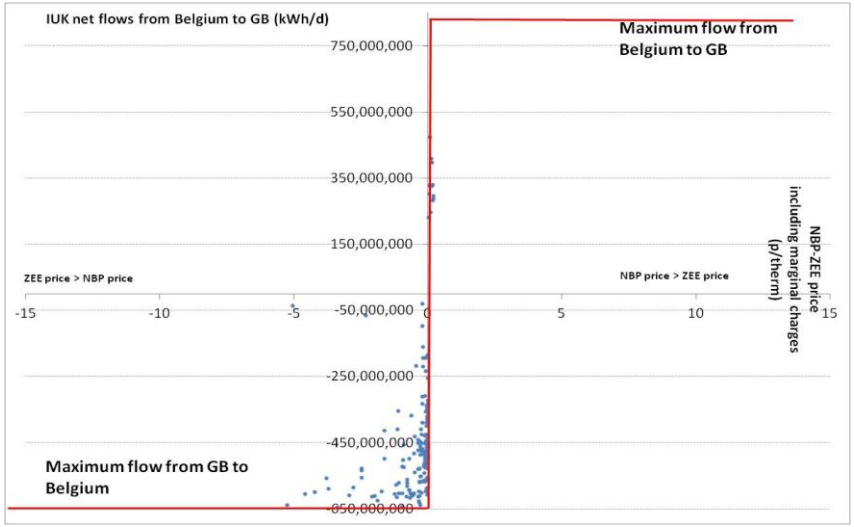
IUK Further Analysis (2)

Gas at neither hub:
((NBP-Commodity Charge) – (Zee - Short Haul Tariff – IUK Fuel Charges)) vs IUK Flows.

When marginal charges less than market spread.

Subtract from the spread the following charges:
i) Where NBP is greater than Zee: Electricity and Bacton gas compressor charges and UK Entry Commodity Charge (only when aggregate charges cost exceeds hub price spread).
ii. Where Zee is greater than NBP, Fuel gas and Bacton gas compressor charges and UK Exit Commodity Charge (only when aggregate charges cost exceeds hub price spread).
iii. Otherwise nothing.



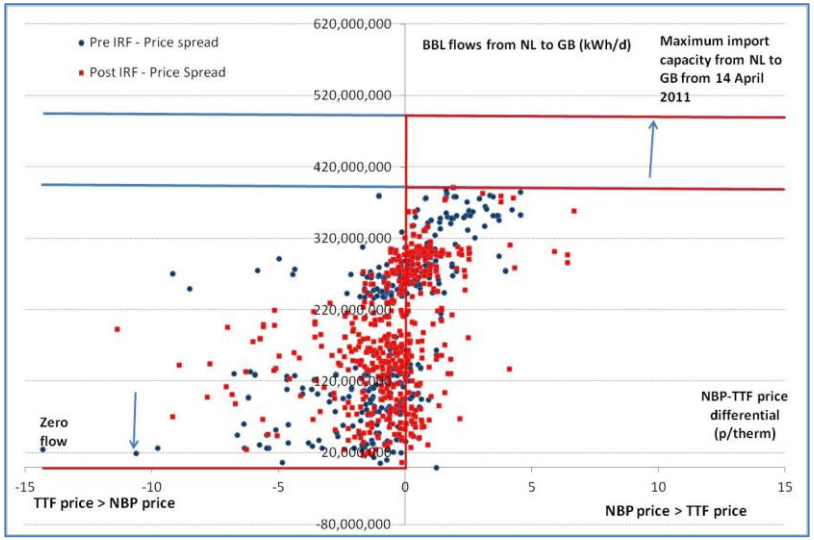


1. Bias to GB has largely disappeared.
2. FAPDs down from 27 % to 9%

FPADs eliminated ... 83 % hub prices converged to less than costs of flow

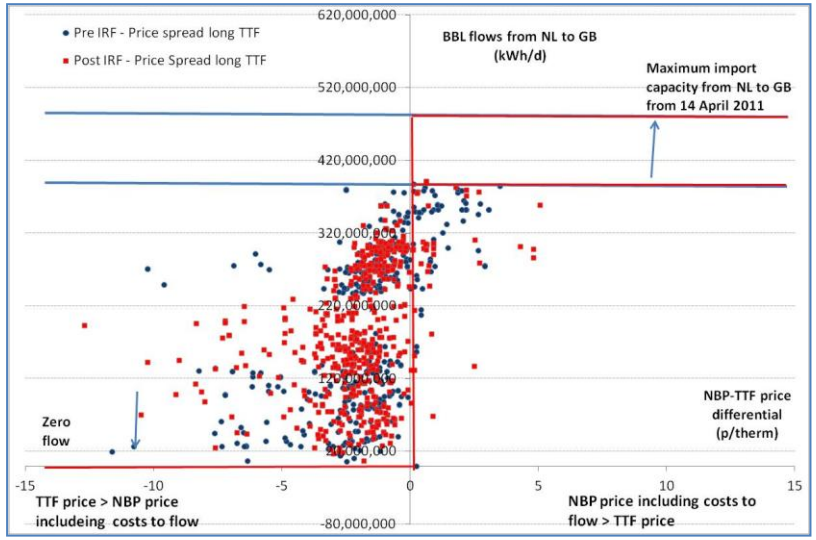
BBL Further Analysis (1)

NBP – TTF vs Flows



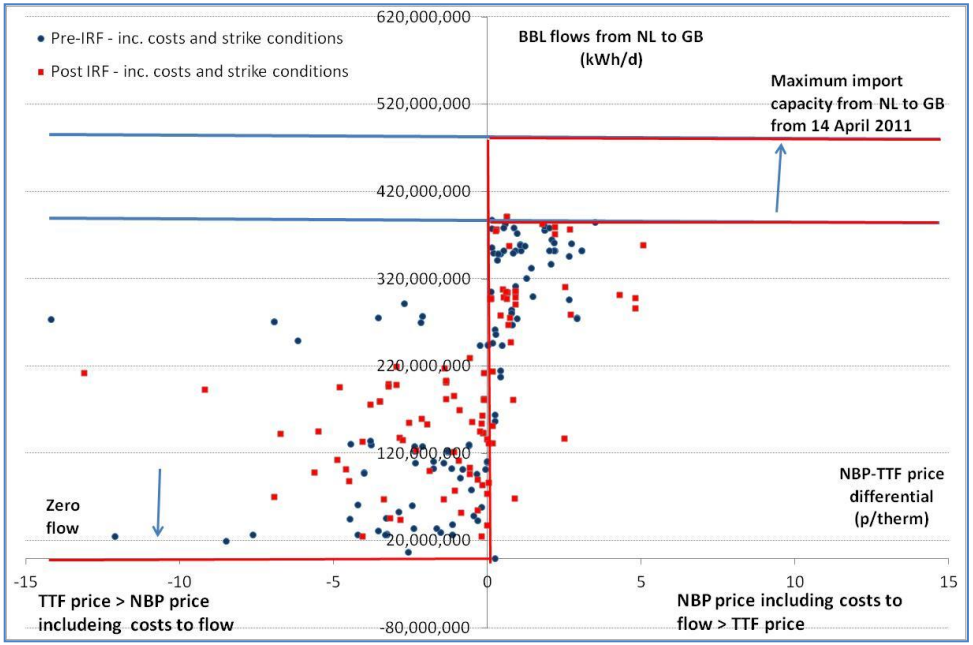
- Correlation using different data source not suddenly apparent ...
- Before IRF FAPD 60% of the time, after 58%.

Shipper long at TTF



- Flow efficiency worsens ...

Flows, only when marginal charges less than market spread



- Even just taking account of days when clear price signals picture remains the same. Still FAPD 54% of the time.
- Markets still converged to less than the value of the costs of flow 69% of the time however.

Final thoughts

- IUK shows a good degree of price responsiveness but low capacity utilisation
- BBL less price responsive
- Key for the charging review discussed today:
  - the current commodity charging regime affects interconnector flows, and tends to encourage the export of gas

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